**STATE OF CALIFORNIA**
**ENERGY RESOURCES CONSERVATION**
**AND DEVELOPMENT COMMISSION**

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| In the Matter of:<br><br>The Preparation of the<br>2005 Integrated Energy Policy Report | Docket 04-IEP-1K<br><br>Notice of Committee Hearings and<br>Availability of the Committee Draft<br>Energy Report |



# COMMENTS OF MERCED IRRIGATION DISTRICT AND MODESTO IRRIGATION DISTRICT ON DRAFT 2005 INTEGRATED ENERGY POLICY REPORT

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On September 15, 2005, the California Energy Commission ("CEC") gave notice of the availability of the Draft 2005 Integrated Energy Policy Report ("Draft Report") and requested that interested parties file comments on the Draft Report by October 14, 2005. Merced Irrigation District ("Merced ID") and Modesto Irrigation District ("Modesto ID") (collectively "the Districts") file these Comments pursuant to that notice.

These comments focus on the discussion concerning departing load appearing at pages 48-49 of the Draft Report. The Districts urge the CEC to be cautious in adopting the current Investor Owned Utility ("IOU") party line in favor of stranded cost charges to departing load, including municipal departing load ("MDL"). There is a serious issue as to whether the CPUC has authority to impose such stranded cost charges. History also shows that the IOUs *can* forecast departing load, and recently adopted AB 1723 *requires* that they (and most Publicly Owned Utilities ("POUs")) provide relevant forecasts regarding load departure. It is more equitable to use such forecasts to plan for MDL load than it is to impose stranded cost charges on such load. Finally, an ambiguity caused by use of the term "departing load" when the term should be "direct access," appearing in a discussion of "coming and going rules," should be corrected.

## *I. Background Regarding The Districts.*

Merced ID has been involved in the electric industry for over 70 years. It has generated wholesale electrical power at its hydroelectric facilities, consisting of two plants at the New Exchequer and McSwain Dams on the Merced River and three mini-hydroelectric plants in irrigation canals, for over 70 years. These resources generate an average of almost 360,000 megawatt hours per year. That power is presently sold to PG&E, who in turn sells it to customers at substantially higher rates. The contract for such sale expires in 2014. Since 1996, pursuant to longstanding statutory authorization, Merced ID has distributed to retail customers (including both new and transferred MDL) power it purchases pursuant to secure long-term and flexible short-term agreements, currently serving 70 megawatts (MW) of peak retail load. Merced ID is unique among publicly-owned utilities in California, because the areas where Merced ID serves customers are completely encompassed in PG&E's historic service area. As a result, Merced ID and PG&E compete head to head, especially for new load located in places that have never before taken electrical service from any utility, including PG&E. Imposition of charges such as stranded cost charges on Merced ID's customers threaten Merced ID's ability to continue providing electric service.

The desire to develop the economic potential of the Merced area is a key factor that spurred Merced ID to enter the retail electric business. The Merced area is one of the most economically depressed areas of the state. One of Merced ID's goals in serving retail customers has been to provide low cost, reliable service in an effort to promote economic growth in Merced County, consistent with local planning policies.

Modesto ID is a publicly owned utility providing electric service to over 105,000 customers within its service area. Modesto ID has provided retail electric service since 1923 and presently serves a peak load of 632 MW utilizing a diverse mixture of owned generation facilities and wholesale power contracts. Modesto ID provided electric service in direct competition with PG&E from 1923 through 1940, when an exclusive service area was established by agreement with PG&E. This agreement's limitations on the Modesto ID electric service area expired in the mid-1950's. Starting in 1995, the neighboring cities of Escalon, Oakdale, Ripon and Riverbank asked Modesto ID to extend electric service to their communities to decrease rates and to improve reliability and customer service. Modesto ID negotiated a new service area agreement and the purchase PG&E electric facilities in these four cities and adjacent rural areas; however the CPUC rejected this agreement by D.98-06-020 to retain the benefits of competition in this area. Pursuant to Public Utilities Code Section 9610(b)(1), effective January 1, 2001, Modesto ID's service area includes over 400 square miles of territory that is also considered part of Pacific Gas and Electric Company's service area, with the result that this portion of the area served by Modesto ID is a non-exclusive service area. Thus, like Merced ID, Modesto ID also competes head-to-head with PG&E for customers in that 400 square mile area. Modesto ID serves approximately 2,000 electric customers with over 60 MW of new and transferred municipal departing load in this joint electric distribution service area. Modesto ID is also interested in economic development in its area and offers an economic development discount rate to qualified customers locating or expanding in the District service territory which create new economic development and job opportunities in the community.

### 2. *Publicly Owned Utilities Are Long-Time Participants in the California Energy Community.*

POUs have existed for decades in California and have during that time presented competitive alternatives to IOUs. POUs can be organized under different authorizing statutes, but may be broadly grouped into two types. The first are those with exclusive service areas. For example, a portion of the area served by Modesto ID is exclusive. These "exclusive POUs" do not compete head-to-head with IOUs for customers, but do compete nonetheless, since when potential customers are making business or personal location decision, they can and do consider issues such as availability and reliability of service and price. The second are those with non-exclusive service areas, who do compete head-to-head with an IOU for customers. As discussed above, all the area served by Merced ID is non-exclusive, as is a portion of the area served by Modesto ID. To the Districts' knowledge, they are the only two such POUs in California.

The CEC should be careful about recommending policies that favor one sort of utility over another. POUs are long-standing members of the retail energy supply community in California and provide valuable service to their customers. Policies that would threaten their existence or provide a competitive advantage to IOUs over POUs should be avoided. Instead, the CEC should work to adopt or recommend policies that are competitively neutral and equitable. The stranded cost policy recommended in the Draft Report is neither.

### *3. Prudent, Coordinated Planning, Not Automatic Default to Stranded Cost Charges, Is the Best Way to Address MDL.*

#### *a. The Draft Report's Recommended Stranded Cost Policy.*

In a portion of the Draft Report entitled "Uncertainty from Departing Loads," the Draft Report restates IOU concerns that various things, including departure of customers to POUs, create uncertainty in resource planning. The Draft Report then discusses CPUC policies on stranded costs for departing load, and uncritically adopts that policy: "The Energy Commission agrees with the CPUC's conclusion that establishing exit fees for departing load is the most equitable approach for meeting the goal for providing 'the need for reasonable certainty for rate recovery' as well as ensuring that California meets its energy needs. The Energy Commission believes that the CPUC policy of establishing exit fees is sufficient to eliminate the lion's share of uncertainty about departing load." (Draft Report, p. 48 (footnote omitted).)

The Districts strongly disagree with the Draft Report's conclusion, which is accompanied by no critical or objective analysis, that stranded cost recovery is an equitable way to address departing load issues. The Districts will now explain their disagreement.

#### *b. There are Serious Legal Issues as to Whether the CPUC has Authority to Levy Generation-Related Stranded Cost Charges.*

First, the Districts note that there are serious legal questions concerning the authority of the CPUC to order stranded cost recovery absent specific legislative authorization. It is well recognized that the CPUC does not have jurisdiction to regulate or fix rates, or impose charges on, the customers of a publicly owned utility unless there has been an express grant of such authority by the legislature consistent with the California Constitution. (Cal. Const., art. 11, § 9, art. 12, §§ 3 and 6; Public Utilities Code § 216; *County of Inyo v. Public Utilities Commission* (1980) 26 Cal.3d 154, 166.) The legislature has granted the Commission only limited power to impose stranded costs on municipal departing load customers, which power was granted in AB 1890. (*See* Public Utilities Code § 367.) The bounds of that power are very carefully and narrowly crafted. No stranded costs can be imposed on municipal departing load customers except as set forth in AB 1890. The CEC should be cautious about recommending a policy the legal basis of which is so open to question.

***c. It Is Not Only Better to Plan for Load Movement, It Is Now Legally Required that Such Forecasting Occur, and the CEC Plays a Major Role in That Forecasting.***

With virtually no discussion, the Draft Report accepts uncritically the IOUs' cries that they just can't manage to plan for departing load. The Districts urge the CEC to recognize these claims for what they are: not backed up by fact, and part of the arsenal brought to bear by IOUs on competitors.

The facts show that at least as to PG&E, it can and has planned for MDL, as is shown by PG&E's August 2001 Bypass Report concerning MDL, discussed in CPUC Decision No. 04-11-014, which allowed MDL certain exceptions to DWR charges based on the evidence of that Bypass Report. Further, the two largest California IOUs are two of the largest and most sophisticated utilities in the world. A claim they do not have the expertise to forecast departures is entitled to no deference at all. The PG&E Bypass Report shows, in fact, that it does have such expertise.

Further, due to the passage and signing of AB 1723 (Stats. 2005, ch. 703), the IOUs not only have the expertise, they are now required to exercise it – as are, by the way, POUs. Under AB 1723, all retail electricity providers (with the possible exception of POUs who do not plan to expand beyond their existing exclusive service territories) will be legally required to engage in forecasting. AB 1723 adds Section 25302.5 to the Public Resources Code. According to the Legislative Counsel's Digest of the bill:

> This bill would require each entity that serves or plans to serve electricity to retail customers to provide the Energy Commission with its forecast, as part of each integrated energy policy report, of (1) the amount of its forecasted load that may be lost or added by a community choice aggregator, an existing local publicly owned electric utility, or a

newly formed local publicly owned electric utility, and (2) the load that will be served by an electric service provider. The bill would require the Energy Commission to perform an assessment in the service territory of each electrical corporation of the loss or addition of load specified in (1) and submit the results of that assessment to the CPUC. The bill would authorize the Energy Commission to exempt from these forecasting requirements a local publicly owned electric utility that is not planning to acquire additional load beyond its existing exclusive service territory.

Under AB 1723, the IOUs will be legally required to forecast loss of load to POUs and the CEC will then assess that information and report its assessment concerning such loss to the CPUC. Although the statute does not require it, the process could be collaborative such that both POUs and IOUs could "put their heads together" to arrive at the best possible forecast of departures.

Following this course of action is far more equitable than are stranded costs charges for a number of reasons. First, since the departing load would be planned for, power would not be procured for it and no stranded costs charges would be necessary. Second, MDL customers would not be required to pay for power they do not consume and which therefore does not benefit them. Third, it would actually advance the goal of bundled customer indifference. "Indifference" means neither harmed nor favored. Failure to take these legally required assessments into account could result in bundled customers actually being favored by having their rates subsidized by departing customers who could have been planned for. Such subsidization would not be indifference.

In addition, in light of both an ability and a legal requirement to plan for departing load, the IOUs' insistence on stranded cost charges should be seen as what it is: an effort to advance their competitive positions against competitors such as POUs. The current rationale for stranded cost recovery is to avoid cost-shifting from departing load to bundled customers, but brief analysis shows the concern over cost-shifting to be selective at best. The IOUs do not seek to impose stranded cost charges for their generation assets on a customer who moves to another California IOU's service territory. The IOUs do not seek to follow a customer who moves to Oregon or Ohio or Guam with a claim that the customer owes stranded costs. To state a somewhat ridiculous example, the IOUs do not assert that when a customer dies, that customer's estate owes a stranded cost charge. But customers do migrate to other IOU territories or move out of state or die. When they do, costs are left behind, and other customers have to bear them. For some reason, the IOUs are very concerned that a customer who leaves for a competing POU must pay a stranded cost charge, claiming that without such a charge cost shifting will occur. The reason is obvious: the IOUs are not worried about other California investor owned utilities and know just how absurd it would be to try to chase a customer out of state or make a claim in a decedent's estate for stranded cost recovery. But when IOUs can impose a stranded cost charge on a competitor's customer, thus making the competitor less economically attractive, the IOUs want to and solemnly pronounce that not allowing such a charge to would result in cost-shifting.

In short, the IOUs' anti-competitive agenda is transparent. The CEC should be reluctant to urge the adoption of polices that advance such an agenda.

Finally, the Districts note that under Public Resources Code Section 25301(a) (cited in the first paragraph of the September 15 notice), among the matters to be considered by the CEC are "energy policies that . . . enhance the state's economy, . . .". The Districts each have an interest in economical development in the areas they serve, which are located in an area of the state that historically is economically underdeveloped. Recommending a policy that would result in stranded cost charges that in turn favor the IOUs' anticompetitive goals would be counter to the goal of economic enhancement included in Section 25301(a).[1]

***4. The Draft Report Must Be Revised to Correct an Ambiguity in the Discussion Regarding Coming and Going Rules.***

The Districts' final comments concern an apparent oversight in the discussion of coming and going rules on page 48. Beginning in the fourth paragraph on the page, the Draft Report addresses "'coming and going rules' for *future direct access* . . .". (Italics added.) This discussion continues through the first full paragraph at the top of page 49. However, somehow in the middle of the discussion "direct access" becomes "departing load," and ultimately the Draft Report recommends "that the CPUC begin immediately to establish appropriate going and coming rules for departing load."

The Districts believe the drafters of the Draft Report intended in this discussion to address direct access departing load, not all departing load. Any other interpretation would not make sense, because a person who moves from San Francisco to Modesto or Sacramento for employment reasons, then moves back to San Francisco obviously cannot be expected to comply

1 The Districts note that it is actually Public Resources Code Section 25302(a) that calls for biennial IEPRs. The Districts' point regarding economic concerns still pertains under that section, which calls for the CEC to consider economic impacts of energy issues facing the state.

with coming and going rules. This sort of customer movement has occurred for decades with no call for coming and going rules.

The Districts suggest that the words "departing load" in the fourth, tenth, and eleventh lines on page 49 of the Draft Report be changed to "direct access."

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Respectfully Submitted,

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